

Message Text

LIMITED OFFICIAL USE

PAGE 01 OECD P 03386 01 OF 03 021923Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 USIA-06
OPIC-03 SP-02 TRSE-00 CIEP-01 LAB-04 SIL-01 AGRE-00
OMB-01 XMB-02 STR-04 /091 W
-----021935Z 026004 /43

R 021921Z FEB 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC 5173
INFO AMEMBASSY BERN

LIMITED OFFICIAL USE SECTION 01 OF 03 OECD PARIS 03386

PASS CEA, TREAS, FRB

E.O. 11652: N/A
TAGS: OECD, ECON
SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC)
REVIEW OF SWITZERLAND

1. SUMMARY: IN REFDOC CIRCULATED FOR FEBRUARY 9 EDRC
REVIEW OF SWITZERLAND, SECRETARIAT POINTS TO FOLLOWING
FACTORS WHICH HAVE DOMINATED RECENT EVOLUTION OF SWISS
ECONOMY: (A) LOW LEVEL OF UNEMPLOYMENT (AMONG SWISS)
COMBINED WITH SOCIAL AWARENESS OF DANGER OF INFLATION
FREED SWISS AUTHORITIES TO CONCENTRATE ON REDUC-
ING INFLATION; (B) INTERACTION BETWEEN APPRECIATION OF
SWISS FRANC AND WAGE/PRICE MODERATION HAS HAD CUMULATIVE
IMPACT IN DAMPENING INFLATIONARY PRESSURES;
(C) WIDENING OF CURRENT ACCOUNT SURPLUS RESULTING, IN
PART, FROM WEAK DOMESTIC DEMAND, HAS CONTRIBUTED TO
UPWARD PRESSURE ON FRANC AND (D) DROP IN GROWTH EXCEP-
TIONALLY SHARP (WITH ABSOLUTE REAL GNP DECLINING BY 8
PERCENT OVER LAST 2 YEARS) DUE TO CONFLUENCE OF ADVERSE
CYCLICAL AND STRUCTURAL DEVELOPMENTS. SECRETARIAT PUTS
LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 02 OECD P 03386 01 OF 03 021923Z

SWISS REAL GNP GROWTH AT ABOUT 0.5 PERCENT IN 1976,
FORECASTS RISE OF ONLY 1.5 PERCENT IN 1977, AND EXPECTS
SLOW GROWTH TO BE ACCOMPANIED BY MILD ACCELERATION OF
INFLATION AND SLIGHT WIDENING OF ALREADY SWOLLEN CURRENT
ACCOUNT SURPLUS. SECRETARIAT DEVOTES SECTION OF REFDOC
TO EVOLUTION OF SWISS COMPETITIVE POSITION SINCE 1965
AND CONCLUDES THAT WHILE SWISS RELATIVE COST POSITION

HAS DETERIORATED SINCE 1970, EFFECTS ON TRADE VOLUMES HAS BEEN MODERATED BY SUCH NON-PRICE FACTORS AS PRODUCT QUALITY AND PRODUCT DIFFERENTIATION. SECRETARIAT RECOMMENDS THAT SWISS (A) MAINTAIN EXPANSIONARY MONETARY POLICY IN 1977; (B) MOVE TOWARD INCREASED FISCAL POLICY STIMULUS; (C) GUARD AGAINST EXCESSIVE APPRECIATION OF FRANC; (D) ADOPT EMPLOYMENT (INCLUDING RETRAINING) MEASURES TO ASSIST NECESSARY STRUCTURAL ADJUSTMENT AND (E) DROP SALES TAX IN FAVOR OF VAT.

ACTION REQUESTED: MISSION WOULD APPRECIATE COMMENTS/ QUESTIONS WHICH COULD BE USEFULLY POSED AT REVIEW.

(NOTE: REP FROM EMBASSY BERNE WILL PARTICIPATE IN REVIEW.) END SUMMARY

2. SHORT TERM SITUATION AND PROSPECTS; DOMESTIC SITUATION: SECRETARIAT UNDERLINES SWISS SUCCESS IN REDUCING INFLATION RATE TO 2 PERCENT IN 1976 AND NOTES THAT GOS FLEXIBILITY TO PURSUE ANTI-INFLATION POLICY DERIVED FROM SOCIAL AWARENESS OF DANGER OF INFLATION AND FROM FACT THAT SWISS WERE RELATIVELY UNSCATHED BY RISING UNEMPLOYMENT (WEAKNESS IN LABOR MARKET WAS REFLECTED MAINLY IN DEPARTURE DURING 1975 AND 1976 OF 200,000 FOREIGN WORKERS, OR 6 PERCENT OF ACTIVE POPULATION). SECRETARIAT ADDS THAT INTERACTION BETWEEN APPRECIATION OF SWISS FRANC AND WAGE/PRICE MODERATION PLAYED IMPORTANT ROLE IN CONTAINING INFLATION. SECRETARIAT ESTIMATES THAT REAL SWISS GDP ROSE BY ONLY 0.5 PERCENT IN 1976 WITH FISCAL STIMULUS PROVIDING ONLY SIGNIFICANT SUPPORT TO GROWTH.

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 03 OECD P 03386 01 OF 03 021923Z

3. 1977 OUTLOOK: SECRETARIAT FORECASTS CONTINUING WEAKNESS OF MOST COMPONENTS OF DOMESTIC DEMAND IN 1977 AND REAL GNP GROWTH OF 1.5 PERCENT. NEGLIGIBLE RISE IN HOURLY WAGE RATES AND PROBABLE DECLINE IN EMPLOYMENT WILL RESTRAIN GROWTH OF DISPOSABLE INCOME; LABOR MARKET WEAKNESS WOULD ALSO MILITATE AGAINST DECLINE IN SAVINGS RATE. THUS SECRETARIAT PROJECTS RISE OF ONLY 1 PERCENT IN REAL PRIVATE CONSUMPTION WITH MOST OF INCREASE RESULTING FROM RESTOCKING OF CONSUMER DURABLES AND POSSIBLE CONSUMPTION SPURT AT END OF 1977 IN ANTICIPATION OF VAT (IF APPROVED IN JUNE REFERENDUM, VAT WOULD TAKE EFFECT IN JANUARY 1978). MOREOVER, BECAUSE OF CONTINUED DECLINE IN RESIDENTIAL CONSTRUCTION AND SLOW GROWTH OF BUSINESS INVESTMENT (DUE TO EXCESS CAPACITY AND RISE IN REAL INTEREST RATES) SECRETARIAT FORECASTS 2 PERCENT DECLINE IN GROSS FIXED CAPITAL FORMATION THIS YEAR. FINALLY, SECRETARIAT NOTES THAT SLOW GROWTH OF FINAL DEMAND IMPLIES MODERATE STOCK ACCUMULATION, AND

THAT FISCAL POLICY STIMULUS WILL DIMINISH DURING YEAR,

LIMITED OFFICIAL USE

NNN

LIMITED OFFICIAL USE

PAGE 01 OECD P 03386 02 OF 03 021931Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 USIA-06
OPIC-03 SP-02 TRSE-00 CIEP-01 LAB-04 SIL-01 AGRE-00
OMB-01 XMB-02 STR-04 /091 W
-----021934Z 026097 /43

R 021921Z FEB 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC 5174
INFO AMEMBASSY BERN

LIMITED OFFICIAL USE SECTION 02 OF 03 OECD PARIS 03386

WHILE LITTLE HELP CAN BE EXPECTED FROM GROWTH OF FOREIGN DEMAND. BRIGHT SPOT ON 1977 HORIZON IS PROJECTED INFLATION RATE OF 2-1/2 PERCENT WITH MILD ACCELERATION FROM 1976 PRIMARILY ATTRIBUTABLE TO INCREASE IN PRICE OF PETROLEUM AND FOOD.

4. CURRENT ACCOUNT: SECRETARIAT ESTIMATES THAT SWISS CURRENT ACCOUNT SURPLUS ROSE TO \$3.9 BILLION IN 1976. FOR 1977, SECRETARIAT SEES STRONG DECELERATION IN GROWTH SWISS EXPORT MARKETS AND NOTES LIKELIHOOD THAT SWISS WILL SUFFER LOSS OF MARKET SHARES. SECRETARIAT FORECASTS 4.5 PERCENT GROWTH OF EXPORT VOLUMES COMPARED WITH GROWTH OF 11.5 PERCENT IN 1976. HOWEVER, SECRETARIAT FEELS THAT EXPECTED SLOW GROWTH OF INDUSTRIAL PRODUCTION (2 PERCENT) AND ABSENCE OF SIGNIFICANT STOCK ACCUMULATION WILL RESULT IN GROWTH OF IMPORT VOLUMES OF ONLY 5 PERCENT (VS. 13.6 PERCENT IN 1976). BASED ON EXPECTATION THAT GROWTH OF IMPORT VOLUMES WILL SLACKEN MORE THAN THAT OF EXPORT VOLUMES AND THAT SWISS TERMS OF TRADE WILL IMPROVE, SECRETARIAT FORECASTS CURRENT
LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 02 OECD P 03386 02 OF 03 021931Z

ACCOUNT SURPLUS WILL INCREASE FURTHER TO \$4.2 BILLION IN 1977. SECRETARIAT COMMENTS THAT SWISS WILL BE HARD PRESSED TO COPE WITH UPWARD PRESSURE ON SWISS FRANC IMPLIED BY SURPLUS OF THIS MAGNITUDE.

5. SECRETARIAT DEVOTES SECTION OF REFDOC TO ANALYSIS OF EVOLUTION OF SWISS COMPETITIVE POSITION SINCE 1965 (ON BASIS VARIOUS COMPARATIVE PRICE AND COST CALCULATIONS) AND CONCLUDES THAT (A) SWISS COMPETITIVE POSITION DETERIORATED SERIOUSLY BETWEEN 1970 AND 1976; (B) FROM 1970 TO 1973 DETERIORATION RESULTED FROM WORSENING OF RELATIVE COST POSITION WHICH WAS AGGRAVATED BY FRANC APPRECIATION; WHEREAS BETWEEN 1973 AND 1976 APPRECIATION HAS BEEN EXCESSIVE RELATIVE TO IMPROVEMENT IN COST POSITION; (C) APPRECIATION HAS INTENSIFIED STRUCTURAL PROBLEMS (E.G., IN WATCH INDUSTRY) AND HAS LED TO MODIFICATION OF PATTERN OF OUTPUT IN SEVERAL INDUSTRIES; HOWEVER (D) NON-PRICE FACTORS SUCH AS HIGH QUALITY OF SWISS PRODUCTS, AND FIRMS' ABILITY TO ACHIEVE PRODUCT DIFFERENTIATION HAVE MODERATED MACRO-ECONOMIC EFFECT OF DECLINE IN COMPETITIVENESS; NONETHELESS (E) EXCESSIVE APPRECIATION OF FRANC COULD HAVE SERIOUS CONSEQUENCES.

6. ECONOMIC POLICY: SECRETARIAT NOTES THAT EXPANSIONARY FISCAL POLICY PROVIDED SUPPORT TO GROWTH IN 1976 WITH TOTAL PUBLIC SECTOR DEFICIT REACHING 2.7 PERCENT OF GNP. SECRETARIAT ADDS, HOWEVER, THAT ON ASSUMPTION OF NO CHANGE IN POLICY, FISCAL STIMULUS WILL DIMINISH CONSIDERABLY THIS YEAR.

7. SECRETARIAT STATES THAT GOALS OF SWISS MONETARY POLICY IN 1976 WERE TO LUBRICATE EXPANSION WITHOUT FUELING INFLATION AND TO MINIMIZE UPWARD PRESSURE ON FRANC. GOS SET TARGET OF 6 PERCENT FOR GROWTH OF M1 IN 1976. HOWEVER, BECAUSE OF SUBSTANTIAL INJECTION OF DOMESTIC LIQUIDITY RESULTING FROM OFFICIAL INTERVENTION IN

LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 03 OECD P 03386 02 OF 03 021931Z

EXCHANGE MARKET AND BECAUSE OF SHIFTS FROM M2 INTO M1 INDUCED BY DECLINE IN INTEREST RATES, MONETARY TARGET WAS SUBSTANTIALLY EXCEEDED. SECRETARIAT FEELS THAT 5 PERCENT TARGET SET FOR M1 GROWTH IN 1977 IS APPROPRIATE, BUT DOUBTS WHETHER MONETARY POLICY OR COMPLEX SYSTEM OF CONTROLS ON CAPITAL INFLOWS WILL BE ABLE TO PREVENT FURTHER APPRECIATION OF FRANC THIS YEAR, IN FACE OF LARGE CURRENT ACCOUNT SURPLUS.

8. CONCLUSIONS: BASED ON ANALYSIS REFDON SECRETARIAT
SUGGESTS THAT EDRC REACH FOLLOWING MAIN CONCLUSIONS:

(A) NEITHER FOREIGN DEMAND NOR DOMESTIC DEMAND (GIVEN
UNCHANGED POLICIES) WILL BE SUFFICIENT TO PULL SWISS
ECONOMY OUT OF RECESSION IN 1977;

(B) DESPITE LARGE EXISTING BUDGET DEFICIT, ADDITIONAL
FISCAL STIMULUS, ESPECIALLY AN INCREASE IN PUBLIC
INVESTMENT, WOULD BE APPROPRIATE FROM DOMESTIC AND
INTERNATIONAL STANDPOINT; RELAXATION OF RESTRICTION ON
PUBLIC SECTOR HIRING WOULD ALSO BE DESIRABLE.

(C) SWISS SHOULD FURTHER STIMULATE DOMESTIC DEMAND IN
ORDER TO REDUCE CURRENT ACCOUNT SURPLUS; FURTHER BENE-
FICIAL EFFECT WOULD BE TO MODERATE APPRECIATION OF
FRANC.

(D) STRUCTURAL PORTION OF PUBLIC SECTOR DEFICIT COULD

LIMITED OFFICIAL USE

NNN

LIMITED OFFICIAL USE

PAGE 01 OECD P 03386 03 OF 03 021927Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 USIA-06
OPIC-03 SP-02 TRSE-00 CIEP-01 LAB-04 SIL-01 AGRE-00
OMB-01 XMB-02 STR-04 /091 W
-----021935Z 026142 /43

R 021921Z FEB 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC 5175
INFO AMEMBASSY BERN

LIMITED OFFICIAL USE SECTION 03 OF 03 OECD PARIS 03386

BE REDUCED BY INCREASING ELASTICITY OF TAX REVENUE WITH
RESPECT TO GROWTH OF NATIONAL INCOME. THIS COULD BE
ACHIEVED BY SWITCH FROM SALES TAX TO VAT.

(E) TO ASSIST PROCESS OF STRUCTURAL ADJUSTMENT OVER
MEDIUM TERM SWISS SHOULD MAKE GREATER USE OF SELECTIVE
MANPOWER POLICIES.

9. COMMENT: (A) SECRETARIAT ENUMERATES SEVERAL FACTORS
WHICH IT BELIEVES GAVE GOS FLEXIBILITY TO PURSUE ANTI-
INFLATION POLICY HELPING TO BRING ABOUT REDUCTION OF
INFLATION RATE TO 2 PERCENT IN 1976. IN MISSION VIEW
NEITHER SWISS MONETARY POLICY NOR FISCAL POLICY IN 1976
COULD BE DESCRIBED AS ANTI-INFLATIONARY. MAIN FACTOR
MODERATING PRICE INCREASE APPEARS TO HAVE BEEN APPRECI-
ATION OF SWISS FRANC, A MOVEMENT WHICH GOS TRIED TO
MODERATE. THUS MISSION WOULD QUESTION SECRETARIAT'S
ASSERTION THAT LOW RATE OF INFLATION COULD BE PRIMARILY
ATTRIBUTED TO SUCCESS OF GOS DOMESTIC POLICIES; (B)
SECRETARIAT NOTES THAT INTERACTION OF APPRECIATION AND
LIMITED OFFICIAL USE

LIMITED OFFICIAL USE

PAGE 02 OECD P 03386 03 OF 03 021927Z

WAGE/PRICE MOVEMENTS HAD CUMULATIVE ANTI-INFLATIONARY
IMPACT IN SWITZERLAND. MISSION WOULD NOTE THAT VIRTUOUS
CIRCLE ARGUMENT IS SUBJECT TO SAME CRITICISM AS VICIOUS
CIRCLE ARGUMENTS. MISSION WOULD AGREE HOWEVER THAT IF
EXC-
HANGE RATES OVER-ADJUST VIS-A-VIS RELATIVE COST OR
PRICE MOVEMENTS, THEY CAN HAVE EXOGENOUS EFFECT ON
DOMESTIC INFLATION RATE. IN SWISS CASE IT APPEARS THAT
APPRECIATION MAY BE LINKED TO SWISS COMPARATIVE ADVANT-
AGE AS FINANCIAL CENTER RATHER THAN TO RELATIVE COST
MOVEMENTS AND THUS COULD WELL HAVE HAD EXOGENOUS INFLU-
ENCE ON DOMESTIC PRICES. HOWEVER, SECRETARIAT ANALYSIS
DOES NOT SUPPORT THE CONTENTION THAT VIRTUOUS CIRCLE
WAS OPERATIVE. MISSION PLANS TO MAKE ABOVE POINTS AT
REVIEW; (C) SECRETARIAT SUGGESTS THAT WIDENING CURRENT
ACCOUNT SURPLUS HAS BEEN SUBSTANTIAL CAUSAL FACTOR IN
APPRECIATION. YET, AT SAME TIME, SECRETARIAT CAUTIONS
SWISS AGAINST FURTHER APPRECIATION BECAUSE OF ADVERSE
EFFECTS ON COMPETITIVE POSITION. MISSION WOULD PROBE
LOGIC OF THIS CONTENTION AND SUGGEST THAT APPRECIATION
COULD BE EXPLAINED MAINLY BY CAPITAL ACCOUNT DEVELOP-
MENTS.
KATZ

LIMITED OFFICIAL USE

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: REPORTS, ECONOMIC CONDITIONS, COMMITTEE MEETINGS
Control Number: n/a
Copy: SINGLE
Sent Date: 02-Feb-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977OECDP03386
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D770037-0692
Format: TEL
From: OECD PARIS
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770281/aaaactmr.tel
Line Count: 324
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: d9cdcdcc-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 6
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 28-Feb-2005 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3430690
Secure: OPEN
Status: NATIVE
Subject: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC) REVIEW OF SWITZERLAND
TAGS: ECON, SZ, OECD, EDRC
To: STATE
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/d9cdcdcc-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009